

- (e) The value of donated goods or services of a type not consistent with the definition given shall not be included as operating expenses (e.g., donated services of individuals, such as volunteers, students and trustees).

6.7 Accrual accounting

In order to provide the necessary completeness, accuracy and meaningfulness in reporting data, the accrual basis of accounting is required. Accrual accounting is the recognizing and recording of the effects of transactions and other events on the assets and liabilities of the hospital entity in the time periods in which they apply rather than when cash is received or paid.

6.8 Accounting for minor moveable equipment

- (a) Minor moveable equipment includes such items as waste baskets, bed pans, silverware, mops, buckets, etc. The general characteristics of this equipment are:

1. In general, no fixed location and subject to use by various departments within a hospital;
2. Comparatively small in size and unit cost; and
3. Generally, a useful life of less than three years.

TN 93-11 Approved Date MAR 23 1993

Supersedes TN 89-11 Effective Date MAR 12 1993

OFFICIAL

93-11-MA(NJ)

(b) There are three ways in which the cost of minor moveable equipment may be recorded:

1. The original cost of this equipment may be capitalized and not depreciated. Any replacement of or additions to this base stock would be charged to operating expense.
2. The original investment in this equipment may be capitalized and written off over three years. All subsequent purchases shall be written off over three years.
3. All purchases of minor equipment may be capitalized and depreciated over their estimated useful lives.

(c) Once a hospital was elected one of these methods, that method must be used consistently thereafter.

6.9 Accounting for capital facilities costs

- (a) Capital Facilities include owned or leased land, land improvements, buildings, fixed equipment, leasehold improvements, major moveable equipment and related debt service requirements.
- (b) Land improvements include paving, tunnels, underpasses, on-site sewer and water lines, parking lots, shrubbery, fences, walls, etc. (if replacement is the responsibility of the hospital).

TN 93-11 Approval Date MAR 23 1993
Supervised By 89-11 Effective Date MAR 12 1993

93-11-MA(NJ)

OFFICIAL

- (c) Buildings include the basic walled structure or shell of a hospital and additions thereto.
- (d) Fixed Equipment and Building Components include roofs and attachments to buildings such as wiring, electrical fixtures, plumbing, elevators, heating systems, air conditioning systems, etc. The general characteristics of this equipment are:
1. Affixed to the building and not subject to transfer of movement;
 2. Used for general purpose rather than for specific department functions.
- (e) Leasehold improvements include betterments and additions made by the tenant to the leased property. Such improvements become the property of the lessor after the expiration of the lease.
- (f) Major moveable equipment is that equipment which usually was a relatively fixed location in the building, but is capable of being moved, generally was a specific function related to cost center functions, and was a life expectancy of at least three years.
- (g) Debt service requirements are principal and interest on buildings, fixed equipment, land, land improvements, leasehold improvements, and capitalized renovations as well as escrow payments, in addition

TN 93-11 Approval Date MAR 23 1993
Supervisor 89-11 Effective Date MAR 12 1993

93-11-MA(NJ)

OFFICIAL

to principal and interest required under the terms of a mortgage, but not including operating expenses as defined by GAAP and lease payments required for leased assets capitalized in accordance with the GAAP.

1. Classification of Fixed Asset Expenditures: Assets and related liabilities, as defined above, must be recorded in Unrestricted Funds, since segregation in a separate fund would imply the existence of restrictions on the use of the asset. This includes the costs of construction in progress.
2. Basis of Valuation: Property, Plant, and Equipment, whether owned or leased, must be reported on the basis of cost. Cost shall be defined as historical cost or fair market value at the date of bequest in the case of donated property.
 - i. Interest and capitalization on site preparation costs associated with borrowings for, or purchase of, major moveable equipment shall be included with the cost of the equipment.
3. Accounting Control: To maintain accounting control over capital assets of the hospital, a plant asset ledger should be maintained as part of a hospital's general accounting records. Some items of equipment shall be treated as individual units within the plant ledger when their individuality and unit cost justify such treatment. Other items of equipment, if they are similar and

TN 93-11 APR 1 1993 MAR 23 1993 93-11-MA(NJ)
Superseded by 89-11 Effective Date MAR 12 1993 **OFFICIAL**

are used in a single cost center, may be grouped together and treated in a single unit within the ledger so long as such items are depreciated in a manner equivalent in result to individually depreciating each item.

4. Capitalization Policy:

- i. If an asset has, at the time of its acquisition, an estimated useful life of greater than three years and a historical cost in excess of \$300.00, its cost must be capitalized.
- ii. If an asset does not meet the above criteria, its cost must be recorded as an expense in the year it is acquired. Alterations and renovations which are in excess of \$300.00 and which extend the life of the asset renovated a minimum of three years must be capitalized. Alterations and renovations that do not meet the above criteria shall be reported as operating expense under repair and maintenance costs in the current period.
- iii. The following shall be the required Capitalization Policy for the reporting assets acquired (and renovations per (g)6 below, subsequent to a hospital's Medicaid Schedule of Rates. Assets acquired prior to this date shall be reported in accordance with Generally Accepted Accounting Principles (GAAP).

TN 93-11 Approval Date MAR 23 1998
Supersedes TN 89-11 Effective Date MAR 12 1993

93-11-MA(NJ)

OFFICIAL

5. Interest Expense During Period of Construction: Frequently, hospitals borrow funds to construct new facilities or modernize and expand existing facilities. Interest costs incurred during the period of construction must be capitalized as part of the cost of the construction for reporting purposes. The period of construction is considered to extend to the date the constructed asset is put into use. When proceeds from a construction loan are invested and income is derived from such investments during the construction period, the amount of interest expense to be capitalized must be reduced by the amount of such income.

6. Depreciation Policies:

- i. Depreciation allowances generated from assets used in the hospital's operations are to be reported as an operating expense in the unrestricted funds. Straight-line depreciation must be reported for all assets, with replacement cost provisions (subject to appropriate planning requirements) and debt service requirements for capital assets utilized for Services Related to Patient Care provided in section 5.13.
- ii. The estimated useful life of a depreciable asset is its normal operating or service life in term of utility to the hospital. Some factors to be considered in determining useful life include normal wear and tear, obsolescence due to reasonably

TR 93-11
Supersedes TR 89-11 Effective Date MAR 12 1993

MAR 23 1993

93-11-MA(NJ)

OFFICIAL

expected technological advances, climatic or local conditions and the hospital's policy of repair and replacement. Costs of alterations, renovations, etc. over \$300.00 which extend the life of an asset at least three years shall be added on the remaining book value of the altered or renovated asset and depreciated straight-line over the remaining useful life of the asset.

- iii. The preferred depreciation policy for reporting purposes is for hospitals to record one-half year depreciation in the first year an asset is acquired and one-half year depreciation in the last year of the asset's useful life, but that buildings or major renovations be depreciated based on the month first put into use. However, any depreciation policy consistent with GAAP is acceptable.
- iv. When an asset is retired, the difference between its book value (historical acquisition cost plus capitalized renovations less accumulated depreciation) and its net salvage value shall be recorded as an adjustment to that year's depreciation expense in the cost center or classification to which the asset was assigned.
- v. When Major Moveable Equipment has reached its useful life, but remains in use, its historical cost and accumulated depreciation may be retained in the accounting records by

TN 93-11 Approved Date MAR 23 1993
Supersedes TN 89-11 Effective Date MAR 12 1993

93-11-MA(NJ)

OFFICIAL

department. However, hospitals must be able to report fully depreciated assets separately from those which are not fully depreciated.

7. Debt Financing for Plant Replacement, Renovation and Expansion purposes:

i. Debt financing for capital facilities may take many forms. Under the terms of most debt financing agreements, the debtor shall be required to perform or is prohibited from performing certain acts. In many instances, debt financing gives rise to special accounting treatment because of discounts and premiums on bond issues, financing charges, formal restrictions on debt proceeds, and sinking and other required funds.

(1) Discounts and Premiums on Bond Issues: Discounts and premiums arising from the issue of bonds shall be amortized over the life of the related issue(s).

(2) Financing charges: Costs of obtaining debt financing other than discounts (e.g., legal fees, underwriting fees, special accounts costs) shall be reported as deferred costs and amortized over the life of the related debt.

TN 93-11 Approved Date MAR 23 1999
Supersedes TN 89-11 Effective Date MAR 12 1993

93-11-MA(NJ)

OFFICIAL

- (3) Reporting of Debt Proceeds: Debt agreements for financing plant replacement and expansion programs may or may not require formal segregation of debt proceeds prior to their use. Proceeds which are not required to be formally segregated prior to their use shall be reported as other, noncurrent assets in the Unrestricted Fund.

8. Sinking and Other Required Funds:

- i. These funds are usually established to comply with loan provisions whereby specific deposits shall be used to insure that adequate funds are available to meet future payments of:

(1) Interest and principal (retirement of indebtedness funds); or

(2) Property insurance, related taxes, repairs and maintenance costs, equipment replacement (escrow funds).

- ii. Funds of this nature shall also be required to be held by trustees outside the hospital. Income generated from the investment of such funds may be immediately available to the hospital or such income may be held by the trustee for some future designated purpose.

TN 93-11 MAR 23 1999
Supersedes TN 89-11 Effective Date MAR 12 1993

93-11-MA(NJ)

OFFICIAL

iii. All internally generating sinking and other required funds shall be accounted for in the following manner:

(1) All fund assets, unless the hospital relinquishes control of the fund through a trustee arrangement, must be recorded in the Restricted Internally Generated Plant Replacement Fund as a long-term investment. Payments to a trustee for sinking fund purposes shall be recorded as reductions in the associated long-term debt.

(2) All income generated from the investment of such funds, except as excluded in (g)8i-iii above, must be recorded as non-operating revenue in this fund, except as required under, "Interest Expense during Period of Construction", (see Section 6.9). Income generated from funds under covenant agreement may be accounted for as an addition to the appropriate restricted fund balance account.

9. Early Debt Retirement:

i. Many bond contracts provide for the calling of any portion or all of the issue at the option of the issuer at a stated

TN 93-11 APR 1993 MAR 23 1993

Supersedes TN 89-11 APR 1993 MAR 12 1993

93-11-MA(NJ)

OFFICIAL